

MEMORANDUM

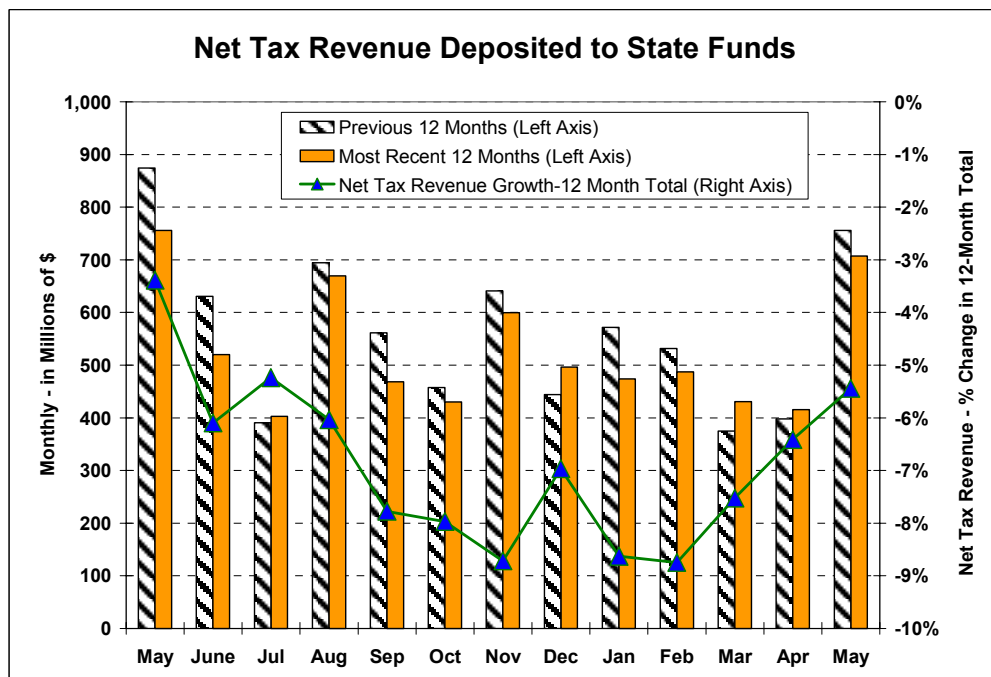
TO: Members of the Iowa Senate and
Members of the Iowa House of Representatives

FROM: Jeff Robinson
Shawn Snyder

DATE: June 25, 2010

Twelve-month Total Net Tax Receipts Through May 31, 2010

The attached spreadsheet presents net tax revenue deposited to State funds for the 12-month period ending May 2010 with comparisons to the previous twelve months. May 2009 to May 2010 one-month comparisons are also presented. The source of the information is the State accounting system, including non-General Fund accounts. All accounting transactions related to taxes remitted to the State were reviewed, along with the refunds issued against those taxes.



Month of May Comparison

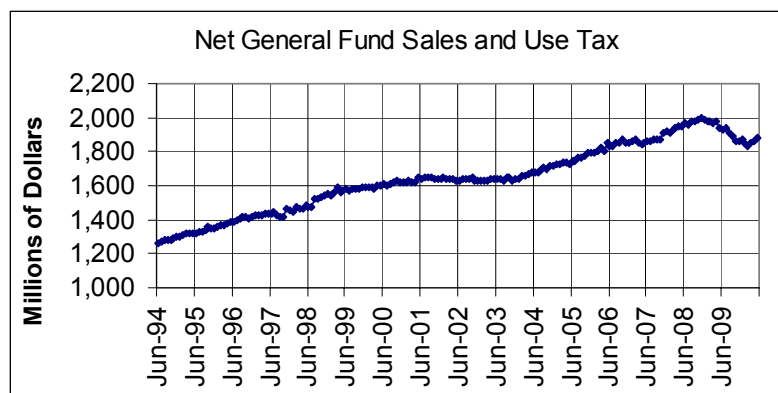
May net tax receipts totaled \$707.7 million, a decrease of \$48.1 million (- 6.4%) compared to May 2009. Major taxes and their contribution to the month's change include:

- Individual Income Tax (negative \$42.6 million, - 12.0%) – Gross income tax receipts decreased \$37.0 million in May while income tax refunds increased \$5.6 million. The large decrease in net revenue was due to significant differences in how tax year 2009 income tax returns were processed this spring compared to last spring.
- Sales/Use Tax (positive \$26.6 million, 10.5%)
 - Road Use Tax Fund use tax/fees for new registrations increased \$4.9 million.
 - Gross General Fund sales/use tax receipts increased \$17.5 million and refunds issued for the month decreased \$4.2 million (net increase of \$21.7 million). This marks the third consecutive month of strong General Fund sales and use tax growth.
- Corporate Income Tax (negative \$28.0 million, - 66.0%) – Gross corporate tax receipts decreased \$9.9 million and refunds increased \$18.1 million.
- Fuel Tax (positive \$3.3 million, 10.5%) – Gross fuel tax revenue increased \$1.1 million while refunds processed in the month decreased \$2.2 million.
- Cigarette & Tobacco Taxes (negative \$1.2 million, - 6.2%) – Cigarette and tobacco tax revenue decreased for the first time in four months.
- Gambling Tax (negative \$0.6 million, - 2.5%) – Total adjusted gross revenue for Iowa's 17 State-regulated gambling facilities decreased 2.1% in May 2010, compared to May 2009, and gambling tax revenue growth has now been negative for 15 consecutive months.

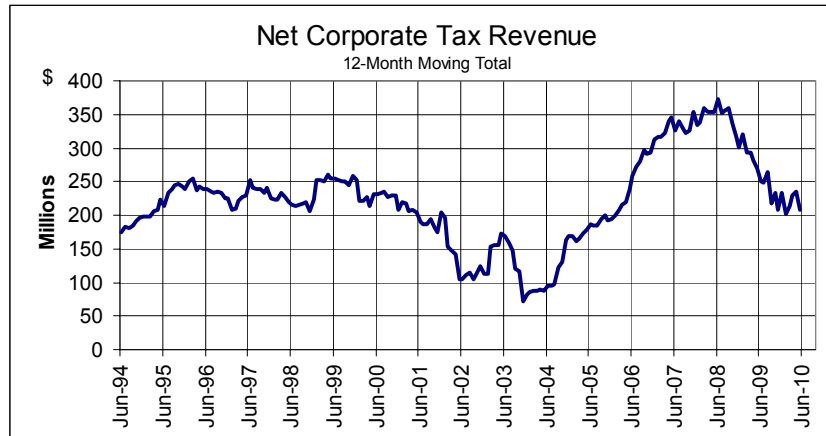
Year-over-Year Comparison – Net Tax Revenue

During the 12-month period ending May 2010, net revenue from all taxes deposited to State funds totaled \$6.101 billion, a decrease of \$351.1 million (- 5.4%) compared to the prior 12 months. Major contributors to the year-over-year dollar and percentage changes include:

- Individual Income Tax (negative \$158.1 million, - 5.7%) – The rate of individual income tax receipt growth peaked in May 2008 at 11.8% year-over-year. The annual growth rate bottomed at negative 9.3% in February 2010 and now stands at negative 5.7%.
- Sales/Use Tax (negative \$73.5 million, - 3.3%) – While the annual growth in sales/use tax revenue is still quite negative, it is a significant improvement from the negative 7.4% over the twelve months ending February 2010. At that point, net sales/use tax revenue was 8.4% below its November 2008 peak.



- Corporate Tax (negative \$62.8 million, - 23.2%) – The May decrease comes after three months of net corporate income tax increases. The most recent twelve months have produced \$207.9 million in net corporate income tax, down \$164.0 million (- 44.1%) from its June 2008 peak. The following chart provides an historical depiction of net Iowa corporate income tax revenue.



- Fuel Tax (positive \$5.5 million, 1.3%) – Net motor fuel tax revenue has been weak the past twelve months, likely the result of decreased economic activity caused by the recession. According to Department of Revenue fuel sales reports, over the most recent 12-month period Iowa taxable gasoline/ethanol gallons sold increased 2.0% while taxable diesel sales were down 3.8%, the nineteenth consecutive month showing a decline in annual taxable diesel sales. Taxable diesel sales over the most recent 12-month period were 10.0% below the March 2008 peak sales level.
- Gambling Tax (negative \$11.6 million, - 4.0%) – Despite expansions of casinos in Clinton and Dubuque, two changes providing boosts to year-over-year gambling growth in Iowa; gambling tax revenue is negative over the past twelve months. According to Racing and Gaming Commission statistics, twelve of Iowa's seventeen casino/track locations reported negative annual adjusted gross revenue (AGR) growth for the 12-month period ending May 2010. The AGR growth for all facilities was negative 3.6% over the past twelve months. Excluding the two expanded facilities, growth was negative 4.6%.
- Cigarette and Tobacco Tax (negative \$14.1 million, - 5.8%) – Economic conditions, Iowa's indoor smoking ban, and an increase in the federal cigarette tax are potential contributors to the tax revenue decline.
- Insurance Premium Tax (negative \$21.6 million, - 21.6%) – The decline in insurance premium tax revenue is the result of expanded use of tax credits, including credits earned through an insurance company's own activities as well as transferable tax credits purchased from others.

Tax Spotlight – Franchise (Bank) Tax and Credit Union Tax

The taxation of banks and financial institutions in Iowa dates back to at least the 1851 [Code of Iowa](#). Prior to HF 1294 (Taxation of Financial Institutions Act of 1970), the bank tax was essentially a property tax, collected and retained at the local level.

The current franchise tax (Iowa Code Chapter 422, Division V) is imposed on the net income of state banks, national banking associations, trust companies, federal and state chartered

savings and loan associations, financial institutions chartered by the Federal Home Loan Bank Board, and production credit associations at a rate of 5.0%. An alternative minimum tax may be applicable to financial institutions at an effective rate of 3.0%. Credit unions are subject to a different tax discussed below.

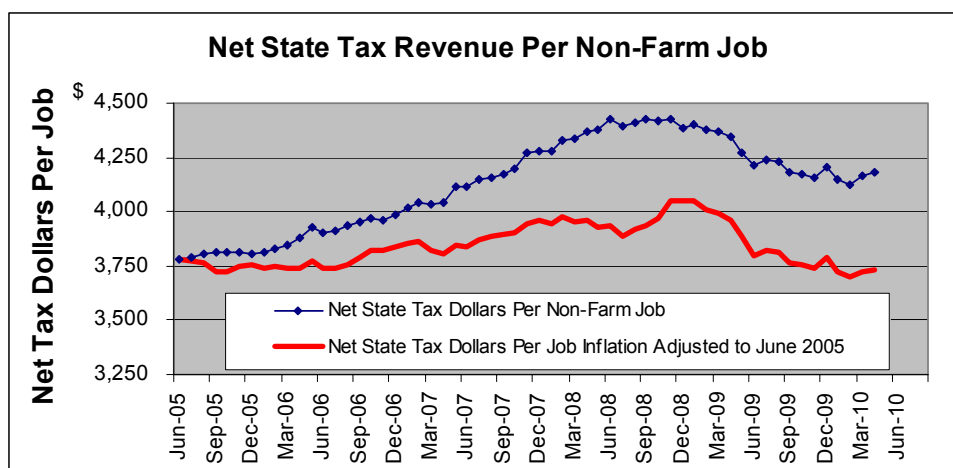
The Iowa franchise tax enacted in 1970 provided for rates ranging from 5.0% to 8.0% of net income. The franchise tax rate was reduced to a flat 5.0% in 1980. Prior to 1995, financial institutions could transfer income-producing assets to non-bank subsidiaries reducing the franchise tax owed. Legislation was enacted beginning with tax year 1995 that prohibits the deduction of those types of transfers.

Tax returns for franchise tax are required to be filed by the last day of the fourth month after the end of the tax year. Estimate payments from most financial institutions are due on a quarterly basis. Revenue received from the franchise tax is deposited in the State General Fund. Iowa Code Section 15F.204(8b) appropriates \$7.0 million of franchise tax receipts annually to the Community Attraction and Tourism Fund through FY 2013, although the appropriation for FY 2011 was eliminated with enactment of SF 2389 (FY 2011 Infrastructure Appropriations Act). The appropriation occurs after the money is deposited to the State General Fund so the franchise tax allocation is essentially a General Fund appropriation.

Credit Unions are taxed at a rate of five mills (0.5%) of “legal and special reserves” (see Iowa Code Section 533.329). The tax is imposed by the Board of Supervisors and the revenue from the tax is divided between the county, city, and State, with the State share equal to 50.0% of revenue collected. The State revenue is deposited to the General Fund.

Tax Revenue and Employment

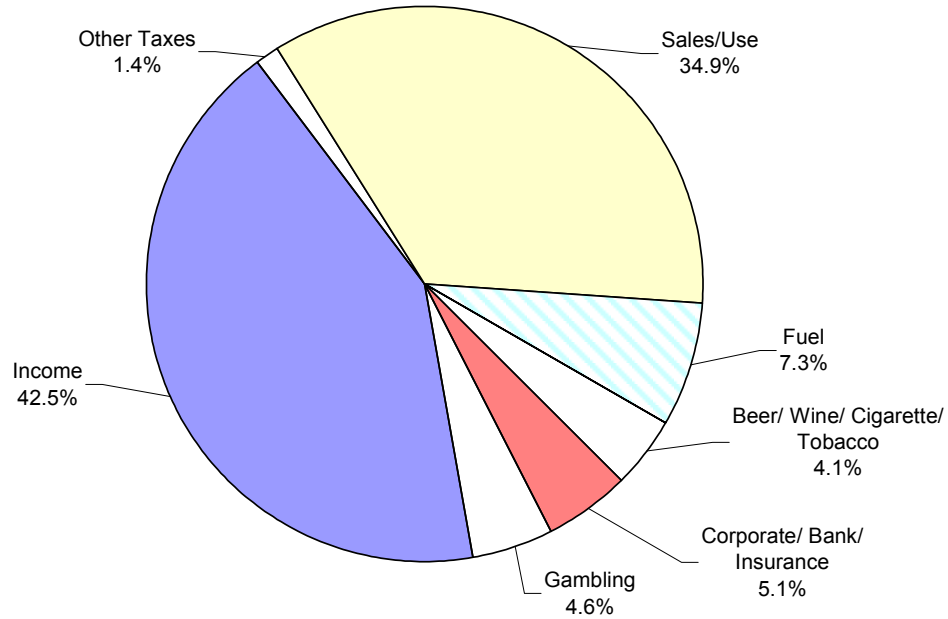
The average reading for Iowa non-farm employment over the 12 months ending April 2010 is 1,470,600, and net State tax receipts over the same twelve months totaled \$6.150 billion, or \$4,182 per non-farm job. This is \$397 (10.5%) higher than the per-job average for the twelve months ending July 2005. Over that same time period, inflation (CPI-U) increased 12.1%. Therefore, tax revenue per job has trailed the rate of inflation since July 2005 by roughly 0.3% per year. The following chart provides a historical perspective of tax collections per non-farm job and inflation-adjusted collections per job.



Net State Tax Revenue - Twelve Months Ending May 2010

Net Revenue = \$6.101 Billion

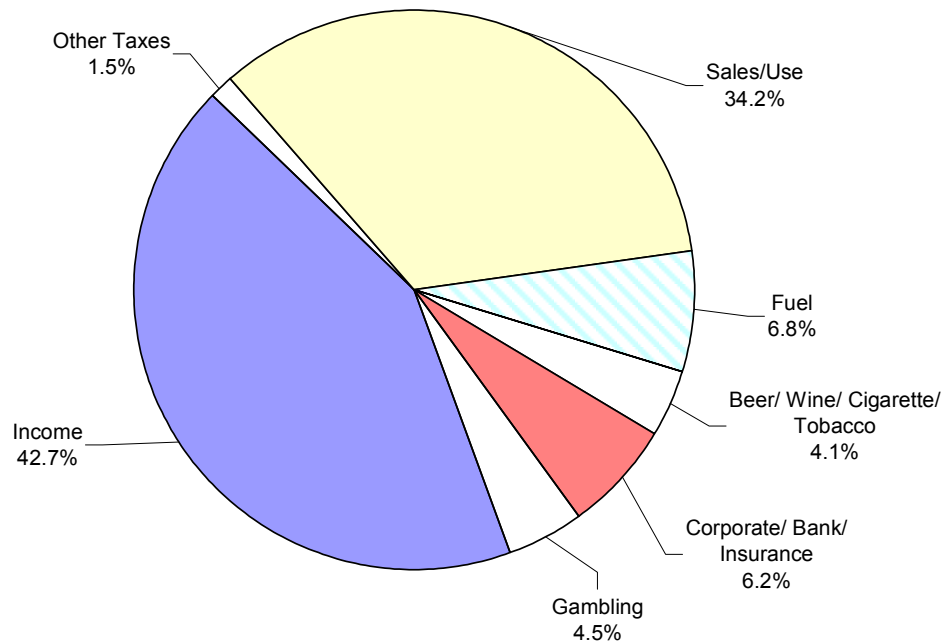
Percentages may not add to 100% due to rounding



Net State Tax Revenue - Twelve Months Ending May 2009

Net Revenue = \$6.452 Billion

Percentages may not add to 100% due to rounding



Net Tax Revenue Deposited to State Funds - Cash Basis

Dollars in millions - Columns and Rows may not add due to rounding

Net Tax by Tax Type	Previous 12-Month Period Total	Most Recent 12-Month Period Total	12-Month \$ Change	12-Month % Change	Month of May 2009	Month of May 2010	May \$ Change	May % Change
Banking	\$ 30.1	\$ 26.8	\$ - 3.3	-11.0%	\$ 3.1	\$ 2.1	\$ - 1.0	-32.3%
Beer & Wine	21.0	21.2	0.2	1.0%	1.7	1.8	0.1	5.9%
Cigarette & Tobacco	241.6	227.5	- 14.1	-5.8%	19.5	18.3	- 1.2	-6.2%
Corporate Income	270.7	207.9	- 62.8	-23.2%	42.4	14.4	- 28.0	-66.0%
Fuel	437.3	442.8	5.5	1.3%	31.5	34.8	3.3	10.5%
Gambling	293.6	282.0	- 11.6	-4.0%	23.8	23.2	- 0.6	-2.5%
Individual Income	2,754.1	2,596.0	- 158.1	-5.7%	353.9	311.3	- 42.6	-12.0%
Inheritance	75.5	66.3	- 9.2	-12.2%	7.5	4.3	- 3.2	-42.7%
Insurance	99.9	78.3	- 21.6	-21.6%	16.9	15.4	- 1.5	-8.9%
Other Taxes	8.8	8.5	- 0.3	-3.4%	- 0.1	0.0	0.1	--
Real Estate Transfer	15.1	12.8	- 2.3	-15.2%	1.3	1.2	- 0.1	-7.7%
Sales/Use	2,204.8	2,131.3	- 73.5	-3.3%	254.3	280.9	26.6	10.5%
Total Net Taxes	\$ 6,452.5	\$ 6,101.4	\$ - 351.1	-5.4%	\$ 755.8	\$ 707.7	\$ - 48.1	-6.4%
Gross Tax & Refunds								
Gross Tax	\$ 7,641.6	\$ 7,382.9	\$ - 258.7	-3.4%	\$ 857.5	\$ 825.9	\$ - 31.6	-3.7%
Tax Refunds	\$ - 1,189.2	\$ - 1,281.6	\$ - 92.4	7.8%	\$ - 101.6	\$ - 118.3	\$ - 16.7	16.4%
Net Tax Receipts by Fund								
State General Fund (GF)	\$ 5,498.7	\$ 5,170.6	\$ - 328.1	-6.0%	\$ 678.4	\$ 622.6	\$ - 55.8	-8.2%
Road Use Tax Fund	\$ 702.7	\$ 697.3	\$ - 5.4	-0.8%	\$ 53.1	\$ 61.3	\$ 8.2	15.4%
Non-GF Gambling	\$ 231.7	\$ 214.4	\$ - 17.3	-7.5%	\$ 23.5	\$ 23.0	\$ - 0.5	-2.1%
Other State Funds	\$ 19.3	\$ 19.1	\$ - 0.2	-1.0%	\$ 0.8	\$ 0.7	\$ - 0.1	-12.5%
Local Option Taxes *	\$ 784.7	\$ 780.4	\$ - 4.3	-0.5%	\$ 65.7	\$ 69.0	\$ 3.3	5.0%

* Sales, income, and hotel/motel. Distributed to local governments - not included in numbers above.

Numbers are rounded to the nearest \$0.1 million. Percentages are calculated after rounding.

Tax Categories Used in Table

Franchise (Bank) Tax: Taxes on banks are deposited to the State General Fund. State credit union tax is included on this line also.

Beer & Liquor Tax: Taxes on beer, liquor, and wine are deposited to the State General Fund, the Liquor Control Fund, and a small amount is deposited to a Department of Economic Development fund for wine promotion.

Cigarette & Tobacco Tax: Cigarette and the tobacco products tax revenue is deposited to the State General Fund.

Corporate Income Tax: All corporate tax is deposited to the State General Fund.

Motor Vehicle Fuel Tax: All motor vehicle fuel tax is deposited to one of two road use funds, with the exception of tax revenue from the sale of aviation and marine fuels.

Gambling Tax: The first \$6.0 million of gambling tax revenue each fiscal year is deposited to the State General Fund (increased to \$66.0 million beginning FY 2010). Other funds receiving deposits of gambling tax revenue over the last 24 months include the School Infrastructure Fund, the Rebuild Iowa Infrastructure Fund, the Gambler's Assistance Fund, the County Endowment Fund, and the Vision Iowa Fund.

Individual Income Tax: Most individual income tax revenue is deposited to the State General Fund. A total of \$4.0 million per year is deposited to the Workforce Development Fund (\$4.0 million). An annual \$2.6 million diversion to the Child Daycare Fund ended in FY 2009. In addition, several economic development programs are financed by individual income tax withholding. In those instances, the employer does not remit the tax withheld from employees and it is never deposited to a State fund. That revenue is not included here.

Inheritance Tax: All inheritance tax is deposited to the State General Fund.

Insurance Premium Tax: All insurance premium tax is deposited to the State General Fund.

Other Taxes: Other taxes include brucellosis eradication property tax (deposited to a Department of Agriculture and Land Stewardship fund), drug stamp tax (State General Fund), utility replacement property tax (State General Fund), and car rental tax (Road Use Tax Fund). Other taxes also include a suspense account used to hold tax deposits prior to determining the correct tax type for the money and tax revenue transferred by the Department of Revenue to separate accounts to fund tax collection activities (tax gap and Department operations).

Real Estate Transfer Tax: Real estate transfer tax is collected by counties. Counties retain 17.25% and remit the remainder to the State. The State deposits 90.0% to the State General Fund, 5.0% to the Housing Trust Fund, and 5.0% to the Shelter Assistance Fund. The distribution of real estate transfer tax revenue changed in FY 2010, when the State General Fund percentage begins a decline to 65.0% by FY 2015.

Sales/Use Tax: General sales/use tax is deposited to the State General Fund, while most vehicle use tax is deposited to the Road Use Tax Fund. Beginning FY 2009, the vehicle use tax was converted to a fee structure. To allow continuity of data, revenue from the fee structure is reflected in this document as tax revenue. Also beginning FY 2009, the School Infrastructure Local Option (SILO) sales tax was converted to a statewide 1.0% sales/use tax and the revenue from that statewide tax is transferred out of the State General Fund monthly through a refund appropriation. To allow for continuity of data, the refund transfers are subtracted as part of the net sales/use tax calculation.

Local Option Taxes: Local option taxes are presented at the bottom of the table and are not included in the numbers above. Prior to FY 2009, local option taxes included the SILO tax, Local Option Sales Tax (LOST) for local government finance, Local Option Income Surcharge for schools, and hotel/motel tax. Starting FY 2009, the SILO tax was converted to a 1.0% statewide tax and the SILO was eliminated. To allow for continuity of data, the transfers from the State General Fund as a result of the 1.0% statewide tax are included in the local option tax amount.

Report Database

The database for this report is the State accounting system. If transactions are incorrectly coded in the system as tax revenue or tax refunds, the numbers presented here will be impacted.